

Economic Conditions Overview and State Revenue Forecast for 2008 and 2009: A Report to the State Funding Board

**By
John Gnuschke, Ph.D., Director
and
Jeff Wallace, Ph.D.,
Research Associate Professor**

**Sparks Bureau of Business and Economic Research,
Fogelman College of Business and Economics**

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- **The risk of a recession is rising nationally and locally.**
- **Economic growth is expected to slow substantially in subsequent quarters.**
- **Third quarter 2007 GDP growth exceeded expectations at 4.9%.**
- **Second quarter GDP also exceeded expectations at 3.8%, while first Quarter GDP growth was 0.6%.**

- **Corporate profits will decline in numerous cyclically-sensitive industries. After dropping 3.8% in Q4 2006, corporate profits grew 1.1% in Q1 2007 and rose by 6.1% in Q2 2007, but fell in Q3 by 1.2%. This is likely to impact Franchise and Excise taxes.**
- **The home market is leading the charge toward a recession. New home sales beginning to stabilize but still substantially lower than last year (as of October).**
- **Sub-prime lending problems and supply glut could depress assessed values, impacting property tax collections.**

- **A disconnect exists between the stock market and real markets.**
- **Despite recent stock market volatility, DJIA is up substantially since December 2006.**
- **Through October, retail sales were growing despite higher fuel and energy prices. While early reports of post-Thanksgiving/Christmas sales were positive, retail sales are expected to slow during the early months of 2008.**

- **Unemployment rates will rise as the economy slows. October Unemployment Rates:**
 - **U.S. = 4.4%, Tennessee = 4.4%, not seasonally adjusted, and**
 - **U.S. = 4.7%, Tennessee = 4.6%, seasonally adjusted.**

- **Consumers drive the economy via retail sales.**
- **Consumer confidence fell for the fourth straight month in November due to a perception of a softening economy, stock market volatility, rising fuel and energy prices, and housing sector woes.**
- **A terrorist strike in the U.S. could have a strong negative impact on U.S. economy. Continued Middle-East conflicts will increase the risk.**

- **Growth in Real Disposable Personal Income (RDPI) growth was flat (but still positive) in the third quarter, negatively impacted by rising food and energy prices.**
- **Outsourcing is expected to continue, impacting the lowest-skilled the most. Areas with undereducated populations (rural and inner-city) will struggle to adapt.**
- **Despite the recent rate cuts, the Federal Reserve keeps a very narrow focus on inflation.**

- **Over production of gas guzzlers, rising health care, and pension costs will continue to eat at the financial health of the Big Three auto makers.**
- **Savings rates are at record lows as consumers finance current expenditures by reducing savings and home equity or going deeper into debt.**

- **Hino Motors expansion in Marion, AR.**
- **Toyota plant opening in Tupelo, MS.**
- **Nucor Steel opening and expanding at the old Birmingham Steel plant in Frank C. Pidgeon Industrial Park.**
- **Major expansion of Gameday-First Tennessee Fields will bring in large numbers of out-of-town visitors.**
- **FedEx hub expansion is expected soon.**

- **Memphis Bio-Tech sector:**
 - **St. Jude expanding, Medtronic Sofomar Danek profitable and expanding.**
 - **Construction has begun on the new UT College of Pharmacy.**
- **FedEx, AutoZone, and other local businesses are profitable. FedEx is growing on international trade and expects record volume during the Christmas shopping season.**
- **Canadian National and BNSF railroads are expanding intermodal and rail services in Memphis.**

- **Sustained higher oil and gas prices driving growth in exploration and alternative fuels (ethanol, biodiesel, etc.). Benefit to agricultural, rail, and trucking companies. Rising transportation costs for others. Rising demand for corn for alternative fuels is leading to increased food costs.**
- **U.S. railroads, FedEx, and UPS (and Memphis) profiting from international trade, weak dollar. China/India buying more U.S. goods and services in return.**

- **Rising violent crime in Memphis and perception of corruption will hamper the ability to attract new and keep existing businesses and residents.**
- **Local October unemployment rates still relatively low: Memphis MSA at 4.9%, City of Memphis at 5.2% (not seasonally adjusted).**
- **The danger of stagnant or even falling property values will hamper the ability of county and municipal governments to meet rising costs in the provision of services and public education.**

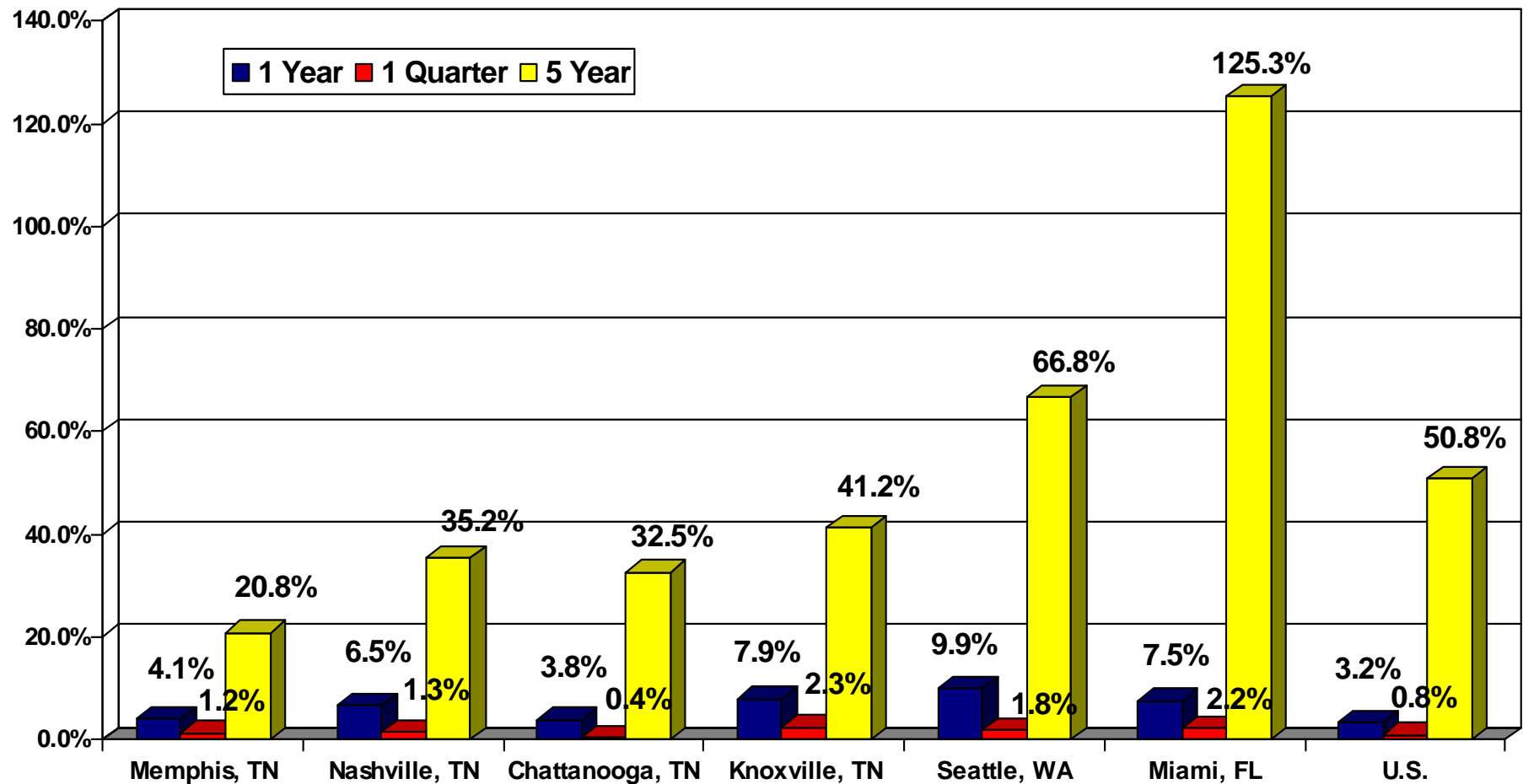
- **No housing bubble in Memphis to bust, but median and average sales price growth is negative. Note, however, that 2006 was a record year.**

Table 1. Home Sales, October 2006 and October 2007

	October 2006	October 2007	Percent Change
Total Home Sales	1,400	1,255	- 10.4%
Median Sales Price	\$135,000	\$123,000	- 8.9%
Average Sales Price	\$173,800	\$148,000	- 14.8%
Monthly Sales Volume	\$243.3 million	\$185.7 million	- 23.7%
Average Time on Market	92.3 days	98.1 days	6.3%

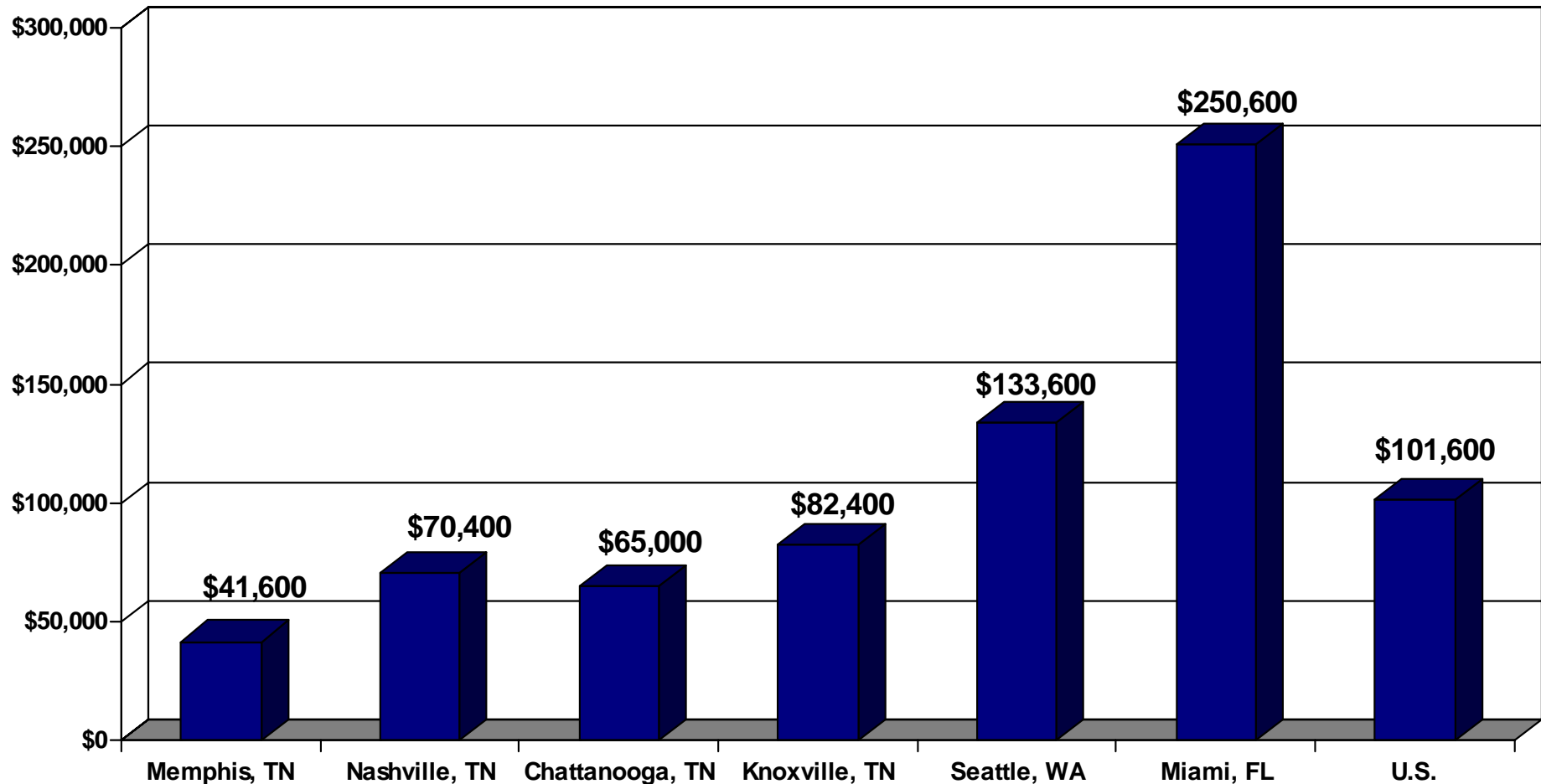
Source: Memphis Area Association of Realtors.

Chart 1. Percent Change in Selected MSA House Prices, As of June 30, 2007



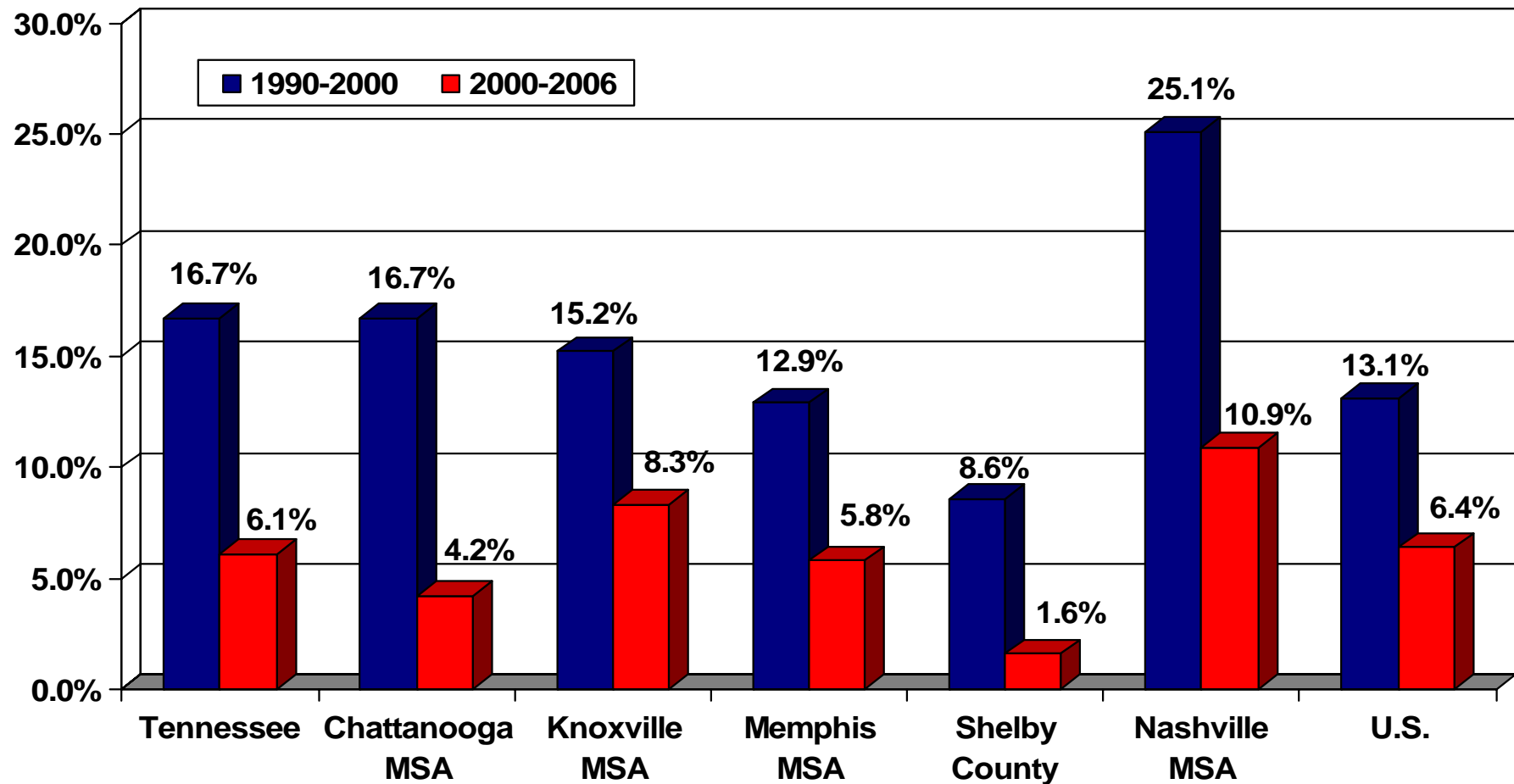
Source: Office of Federal Housing Enterprise Oversight, August 30, 2007.

**Chart 2. Five Year Change on a \$200,000 House,
Selected MSAs As of June 30, 2007**



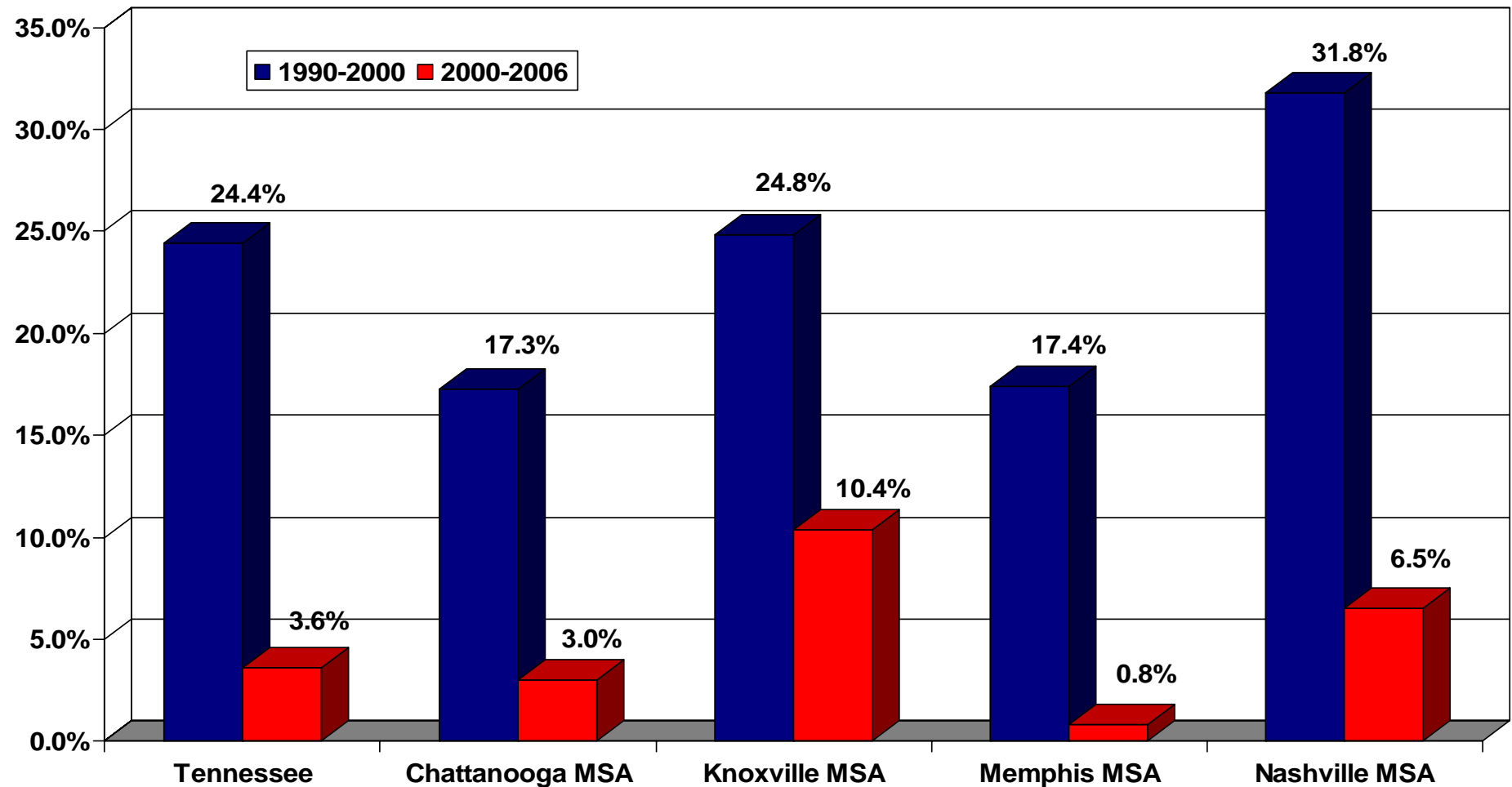
Source: Office of Federal Housing Enterprise Oversight, August 30, 2007.

Chart 3. Population Growth, 1990-2006



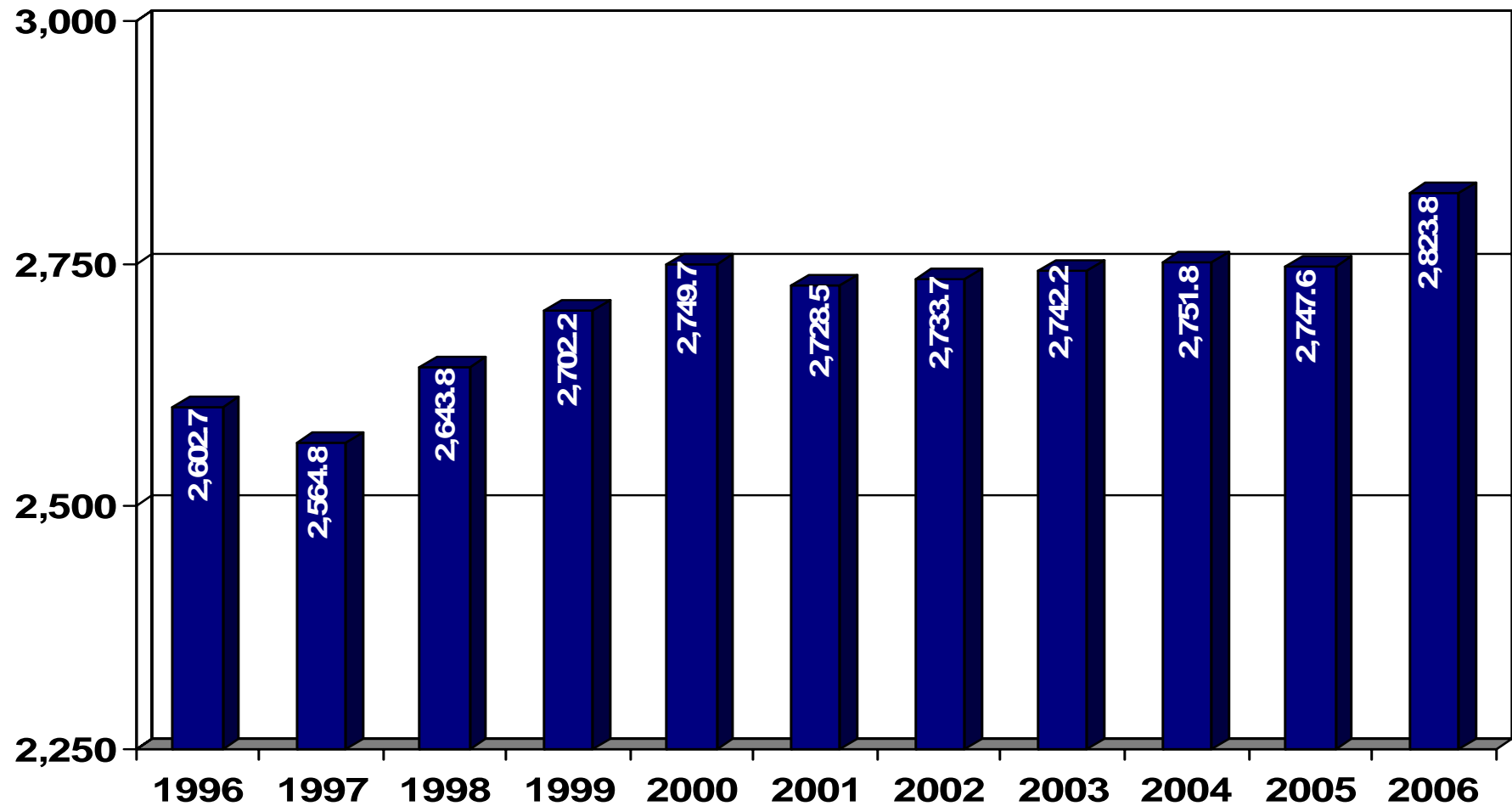
Source: U.S. Census Bureau.

Chart 4. Select Tennessee MSAs' Employment Growth, 1990-2006



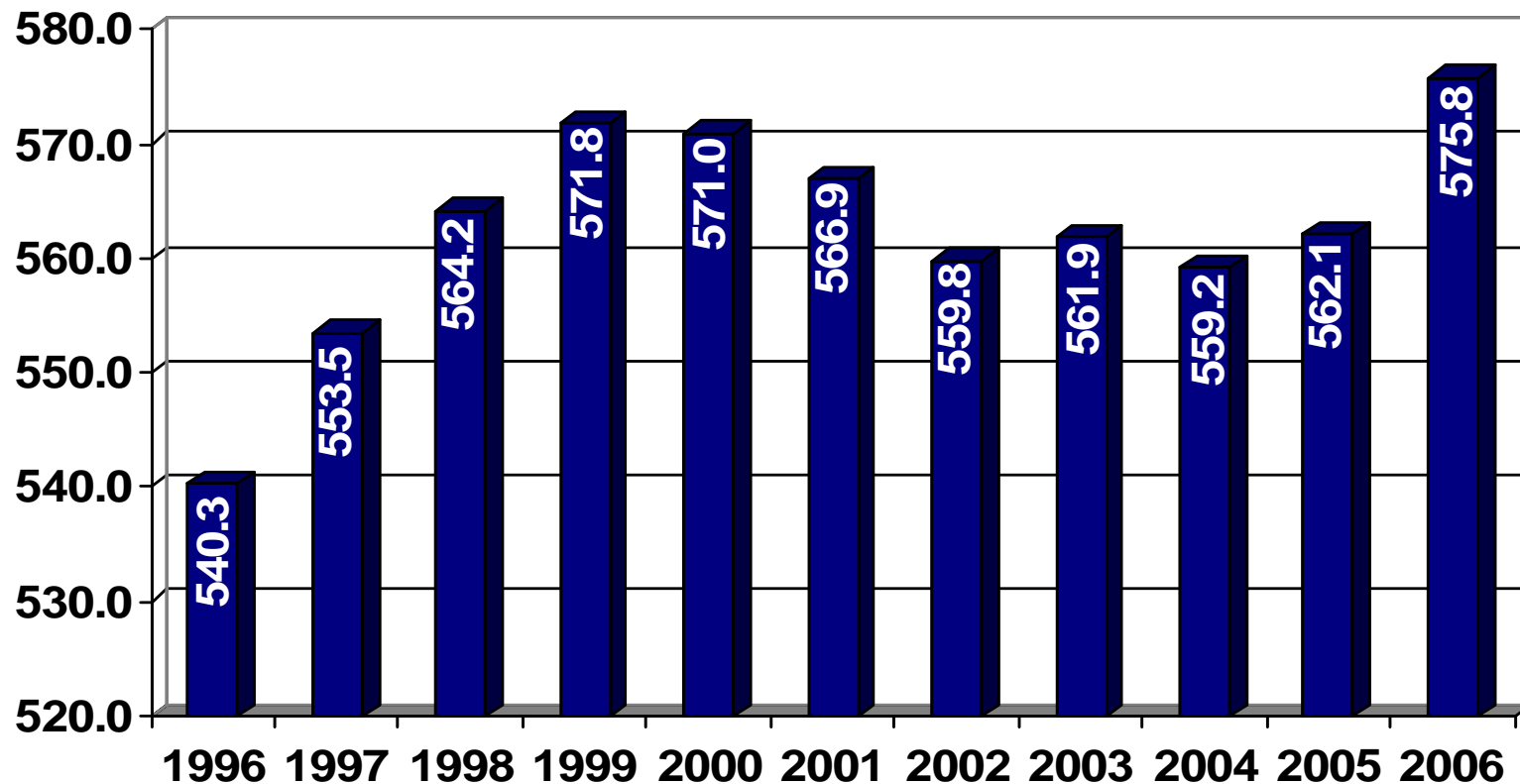
Source: U.S. Bureau of Labor Statistics (residence based).

Chart 5. Employed Tennessee Residents, 1996-2006 (000)



Source: U.S. Bureau of Labor Statistics, Current Population Survey.

Chart 6. Employed Memphis MSA Residents, 1996–2006 (000)

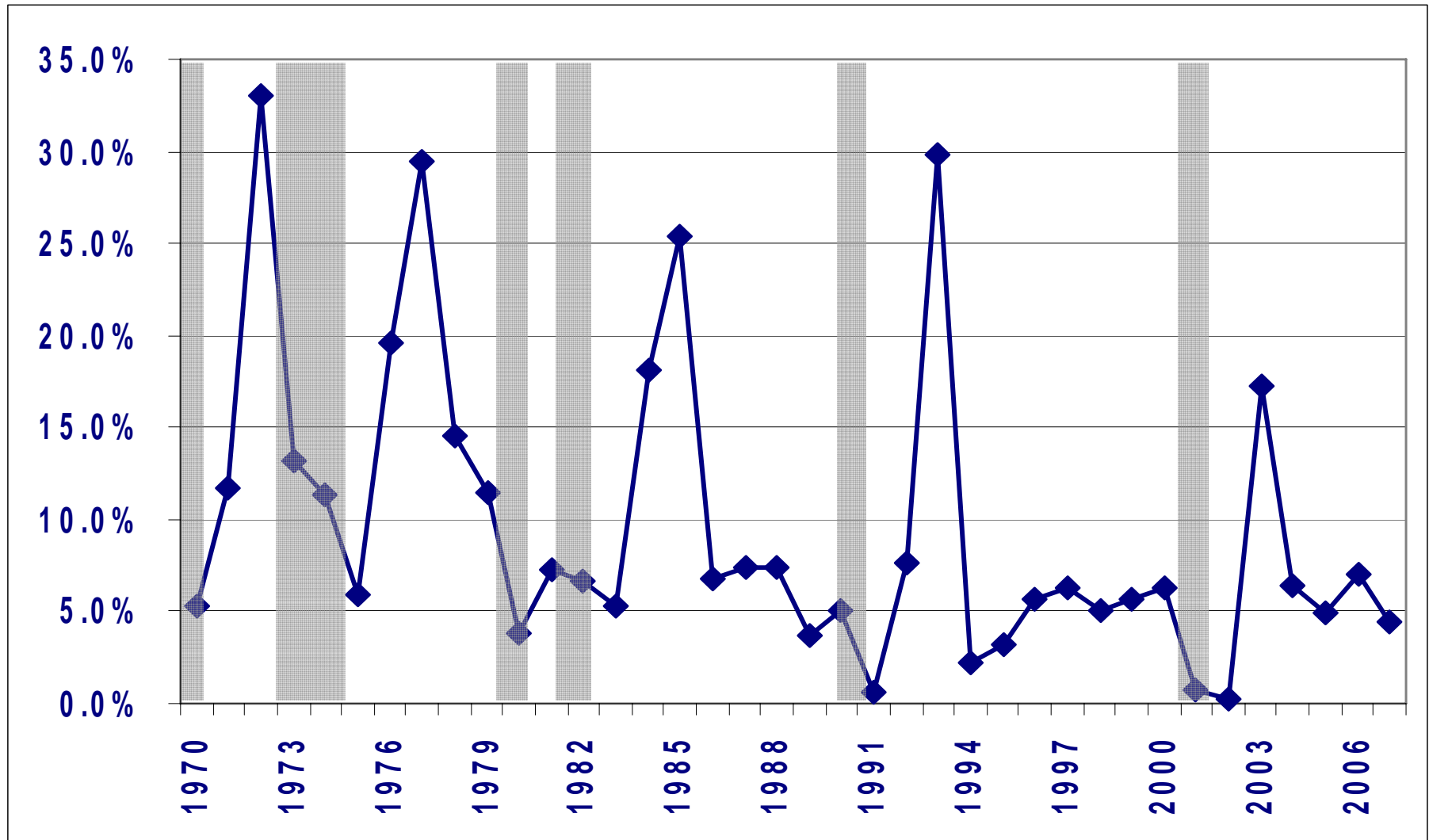


Note: Data is from the Current Population Survey (residence based).

Source: U.S. Bureau of Labor Statistics.

Revenue Forecasts

**Chart 7. Tennessee Sales and Use Tax Collections,
Annual Percent Change 1970-2007**



**Chart 8. Tennessee Total Tax Collections,
Annual Percent Change 1970-2007**

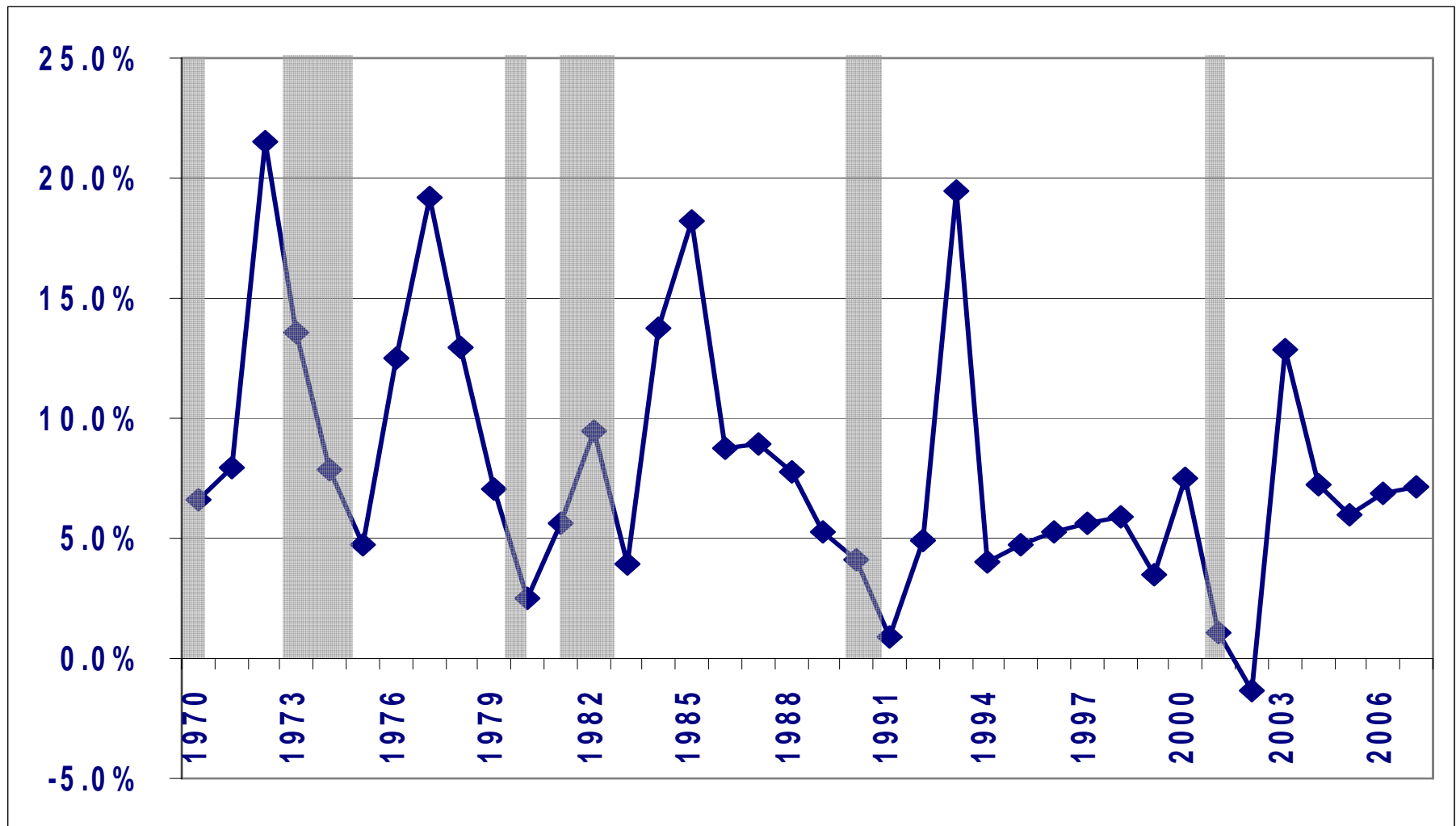


Table 2. Tennessee Accrual Year 2008 Revenue Forecast

Revenue Source	2007 AY	2008 Forecast	Percent Change 08/07
Sales and Use	\$ 6,815,407,300	\$ 7,035,731,128	3.13%
Excise	1,129,107,500	1,207,439,748	6.49%
Franchise	636,972,300	664,071,343	4.08%
Gasoline	612,263,500	635,885,403	3.71%
Privilege	313,793,300	307,849,795	- 1.93%
Gross Receipts	277,617,700	280,720,580	1.11%
Motor Vehicle Registration	257,367,700	266,044,899	3.26%
Income	247,567,500	253,113,977	2.19%
Motor Vehicle Fuel	185,879,400	189,542,803	1.93%
Tobacco	137,933,500	205,933,135	33.02%
Business	133,773,300	135,845,588	1.53%
Inheritance, Gift & Estate	112,393,000	77,916,835	-44.25%
Petroleum Special Tax	65,312,200	66,036,719	1.10%
Mixed Drinks	53,656,700	56,448,924	4.95%
Alcoholic Beverage	40,998,300	43,136,366	4.96%
Beer	17,979,100	18,833,330	4.54%
Motor Vehicle Title	11,105,200	10,932,880	- 1.58%
Coin Amusement & Unauthorized Substances	1,943,400	1,020,127	-90.51%
Combined Severance	1,549,400	1,983,136	21.87%
Total	\$11,052,680,300	\$11,458,486,716	3.54%

Table 3. Tennessee Accrual Year 2008 Revenue Forecast Interval

Revenue Source	25% Lower Bound	2008 Forecast	25% Upper Bound
Sales and Use	\$ 6,994,084,284	\$ 7,035,731,128	\$ 7,077,377,972
Excise	1,166,064,552	1,207,439,748	1,248,814,944
Franchise	647,773,311	664,071,343	680,369,343
Gasoline	628,481,693	635,885,403	643,289,113
Privilege	303,587,378	307,849,795	312,112,212
Gross Receipts	272,866,414	280,720,580	288,574,746
Motor Vehicle Registration	264,663,484	266,044,899	269,472,314
Income	247,840,929	253,113,977	258,387,025
Tobacco	192,605,880	205,933,135	219,260,390
Motor Vehicle Fuel	185,039,909	189,542,803	194,045,697
Business	133,933,097	135,845,588	137,758,079
Inheritance, Gift & Estate	69,391,045	77,916,835	86,442,625
Petroleum Special Tax	65,125,489	66,036,719	66,947,949
Mixed Drinks	56,115,968	56,448,924	56,781,880
Alcoholic Beverage	42,666,671	43,136,366	43,606,061
Beer	18,622,655	18,833,330	19,044,005
Motor Vehicle Title	10,802,418	10,932,880	11,063,342
Combined Severance	1,833,218	1,983,136	2,133,054
Coin Amusement & Unauthorized Substances	240,937	1,020,127	1,799,317
Total	\$11,359,021,999	\$11,458,486,716	\$11,557,951,433

Table 4. Tennessee Accrual Year 2008 Lower Bound Impact

Revenue Source	2008 25% Lower Bound	2007 AY	Percent Change
Sales and Use	\$ 6,994,084,284	\$ 6,815,407,300	2.6%
Excise	1,166,064,552	1,129,107,500	3.3%
Franchise	647,773,311	636,972,300	1.7%
Gasoline	628,481,693	612,263,500	2.6%
Privilege	303,587,378	313,793,300	- 3.3%
Gross Receipts	272,866,414	277,617,700	- 1.7%
Motor Vehicle Registration	264,663,484	257,367,700	2.8%
Income	247,840,929	247,567,500	0.1%
Tobacco	192,605,880	185,879,400	3.6%
Motor Vehicle Fuel	185,039,909	137,933,500	34.2%
Business	133,933,097	133,773,300	0.1%
Inheritance, Gift & Estate	69,391,045	112,393,000	-38.3%
Petroleum Special Tax	65,125,489	65,312,200	-0.3%
Mixed Drinks	56,115,968	53,656,700	4.6%
Alcoholic Beverage	42,666,671	40,998,300	4.1%
Beer	18,622,655	17,979,100	3.6%
Motor Vehicle Title	10,802,418	11,105,200	- 2.7%
Combined Severance	1,833,218	1,943,400	- 5.7%
Coin Amusement & Unauthorized Substances	240,937	1,549,400	-84.4%
Total	\$11,359,021,999	\$11,052,680,300	2.8%

Table 5. Tennessee Accrual Year 2008 Upper Bound Impact

Revenue Source	2008 25% Upper Bound	2007 AY	Percent Change
Sales and Use	\$ 7,077,377,972	\$ 6,815,407,300	3.8%
Excise	1,248,814,944	1,129,107,500	10.6%
Franchise	680,369,343	636,972,300	6.8%
Gasoline	643,289,113	612,263,500	5.1%
Privilege	312,112,212	313,793,300	- 0.5%
Gross Receipts	288,574,746	277,617,700	3.9%
Motor Vehicle Registration	269,472,314	257,367,700	4.7%
Income	258,387,025	247,567,500	4.4%
Tobacco	219,260,390	185,879,400	18.0%
Motor Vehicle Fuel	194,045,697	137,933,500	40.7%
Business	137,758,079	133,773,300	3.0%
Inheritance, Gift & Estate	86,442,625	112,393,000	-23.1%
Petroleum Special Tax	66,947,949	65,312,200	2.5%
Mixed Drinks	56,781,880	53,656,700	5.8%
Alcoholic Beverage	43,606,061	40,998,300	6.4%
Beer	19,044,005	17,979,100	5.9%
Motor Vehicle Title	11,063,342	11,105,200	- 0.4%
Combined Severance	2,133,054	1,943,400	9.8%
Coin Amusement & Unauthorized Substances	1,799,317	1,549,400	16.1%
Total	\$11,557,951,433	\$11,052,680,300	4.6%

Table 6. Tennessee Accrual Year 2009 Revenue Forecast

Revenue Source	2008 Forecast	2009 Forecast	Percent Change 09/08
Sales and Use	\$ 7,035,731,128	\$ 7,284,967,386	3.42%
Excise	1,207,439,748	1,222,352,687	1.22%
Franchise	664,071,343	673,885,791	1.46%
Gasoline	635,885,403	643,596,549	1.20%
Privilege	307,849,795	363,738,748	15.37%
Gross Receipts	280,720,580	283,757,859	1.07%
Motor Vehicle Registration	266,044,899	275,106,892	3.29%
Income	253,113,977	254,012,119	0.35%
Motor Vehicle Fuel	189,542,803	193,210,553	1.90%
Tobacco	205,933,135	200,346,825	- 2.79%
Business	135,845,588	148,939,359	8.79%
Inheritance, Gift & Estate	77,916,835	78,792,517	1.11%
Petroleum Special Tax	66,036,719	66,297,989	0.39%
Mixed Drinks	56,448,924	57,778,187	2.30%
Alcoholic Beverage	43,136,366	44,181,538	2.37%
Beer	18,833,330	18,808,561	- 0.13%
Motor Vehicle Title	10,932,880	11,334,699	3.55%
Coin Amusement & Unauthorized Substances	1,020,127	1,100,000	7.26%
Combined Severance	1,983,136	1,949,268	-1.74%
Total	\$11,458,486,716	\$11,824,157,527	3.09%

Table 7. Tennessee Accrual Year 2009 Revenue Forecast Interval

Revenue Source	25% Lower Bound	2009 Forecast	25% Upper Bound
Sales and Use	\$ 7,242,966,664	\$ 7,284,967,386	\$ 7,326,968,108
Excise	1,180,248,942	1,222,352,687	1,264,456,432
Franchise	657,364,802	673,885,791	690,406,780
Gasoline	636,423,393	643,596,549	650,769,705
Privilege	359,350,483	363,738,748	368,127,013
Gross Receipts	275,886,681	283,757,859	291,629,037
Motor Vehicle Registration	271,660,258	275,106,892	278,553,526
Income	248,695,121	254,012,119	259,329,117
Tobacco	186,921,555	200,346,825	213,772,095
Motor Vehicle Fuel	188,693,305	193,210,553	197,727,801
Business	146,437,297	148,939,359	151,441,421
Inheritance, Gift & Estate	72,624,353	78,792,517	84,960,681
Petroleum Special Tax	65,313,319	66,297,989	67,282,659
Mixed Drinks	57,462,449	57,778,187	58,093,925
Alcoholic Beverage	43,702,101	44,181,538	44,660,975
Beer	18,591,643	18,808,561	19,025,479
Motor Vehicle Title	11,203,604	11,334,699	11,465,794
Combined Severance	1,809,969	1,949,268	2,088,567
Coin Amusement & Unauthorized Substances	334,823	1,100,000	1,865,183
Total	\$11,723,431,612	\$11,824,157,527	\$11,924,883,442

Table 8. Tennessee Accrual Year 2009 Lower Bound Impact

Revenue Source	25% Lower Bound	2008 Forecast	Percent Change
Sales and Use	\$ 7,242,966,664	\$ 7,035,731,128	2.9%
Excise	1,180,248,942	1,207,439,748	- 2.3%
Franchise	657,364,802	664,071,343	- 1.0%
Gasoline	636,423,393	635,885,403	0.1%
Privilege	359,350,483	307,849,795	16.7%
Gross Receipts	275,886,681	280,720,580	- 1.7%
Motor Vehicle Registration	271,660,258	266,044,899	2.1%
Income	248,695,121	253,113,977	- 1.7%
Tobacco	186,921,555	205,933,135	- 9.2%
Motor Vehicle Fuel	188,693,305	189,542,803	- 0.4%
Business	146,437,297	135,845,588	7.8%
Inheritance, Gift & Estate	72,624,353	77,916,835	- 6.8%
Petroleum Special Tax	65,313,319	66,036,719	- 1.1%
Mixed Drinks	57,462,449	56,448,924	1.8%
Alcoholic Beverage	43,702,101	43,136,366	1.3%
Beer	18,591,643	18,833,330	- 1.3%
Motor Vehicle Title	11,203,604	10,932,880	2.5%
Combined Severance	1,809,969	1,983,136	- 8.7%
Coin Amusement & Unauthorized Substances	334,823	1,020,127	-67.2%
Total	\$11,723,431,612	\$11,458,486,716	2.3%

Table 9. Tennessee Accrual Year 2009 Upper Bound Impact

Revenue Source	2009 25% Upper Bound	2008 Forecast	Percent Change
Sales and Use	\$ 7,326,968,108	\$7,035,731,128	4.1%
Excise	1,264,456,432	1,207,439,748	4.7%
Franchise	690,406,780	664,071,343	4.0%
Gasoline	650,769,705	635,885,403	2.3%
Privilege	368,127,013	307,849,795	19.6%
Gross Receipts	291,629,037	280,720,580	3.9%
Motor Vehicle Registration	278,553,526	266,044,899	4.7%
Income	259,329,117	253,113,977	2.5%
Tobacco	213,772,095	205,933,135	3.8%
Motor Vehicle Fuel	197,727,801	189,542,803	4.3%
Business	151,441,421	135,845,588	11.5%
Inheritance, Gift & Estate	84,960,681	77,916,835	9.0%
Petroleum Special Tax	67,282,659	66,036,719	1.9%
Mixed Drinks	58,093,925	56,448,924	2.9%
Alcoholic Beverage	44,660,975	43,136,366	3.5%
Beer	19,025,479	18,833,330	1.0%
Motor Vehicle Title	11,465,794	10,932,880	4.9%
Combined Severance	2,088,567	1,983,136	5.3%
Coin Amusement & Unauthorized Substances	1,865,183	1,020,127	82.8%
Total	\$11,924,883,442	\$11,458,486,716	4.1%